IRS Approves Donor-Managed Account Arrangement—Again

For some time now there has been much attention paid in the financial press and elsewhere to what is said to be a new planned giving vehicle, the donor-managed account. A Connecticut consulting firm obtained a private letter ruling from the IRS approving the concept and is reported to now be applying for a patent on the idea.

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Charitable planners have long worried about gift plans that give the donor continuing control over the assets contributed to a charitable donee. This could cause the gift to be regarded as incomplete (and hence not deductible). Similarly, there have been concerns that the gift tax charitable deduction might be disallowed if the donor has too much control. In PLRs 200445023 and 200445024, however, the IRS held that neither of these problems arose when a college placed contributions into a "donor managed account" which permitted the donor to exercise broad investment authority.

How the Approved College Fund Works

In the approved donor-managed account, the investments in question are placed in a brokerage or investment account in the college's name, and must be used exclusively for the benefit of the college. The donor is allowed to manage the account under a power of attorney that will continue in effect for 10 years. Either party may terminate the arrangement, and the college can withdraw the assets from the account. In the event of "severe losses" (as determined by the college) the arrangement terminates automatically. The donor may select from a variety of investments, including U.S. equities and fixed-income securities, hedge funds, mutual funds, private placements, and real estate investment trusts (REITs). Note: the donor does not have unfettered investment authority. Some actions are prohibited, including self-dealing, short sales, borrowing on the security of the account, investment in derivatives, or voting the securities in the account.

While press reports of the donor-managed account have depicted it as a new innovation in planned giving, planners with a long memory may recall that the IRS approved a very similar arrangement a while back, in 1981. That ruling, PLR 8152072, approved another investment arrangement whereby a donor was entitled to manage investments relating to his contribution (in this case, to a residential care program for youth). The terms of the account in the 1981 ruling were essentially identical to those in the new PLRs, with only a few exceptions. For example, in the earlier ruling the arrangement had a three-year term (instead of 10) and the investments were limited to listed, publicly traded securities. In most respects, however, the old plan was virtually identical to the new one. This, of course, may prove to be an obstacle to the promoter's patent application.

Why Bother?

Why would anyone want to enter into such an arrangement? This question has been raised in the financial press. *Forbes*, for example, described the "new" device in a full-blown article that contended a donor would normally come out ahead simply by holding the contributed securities for the 10-year term and then contributing them, when their value would presumably be greater—as would the donor's deduction. (Ebeling, Ashlea, "Stupid Tax Tricks," *Forbes* (November 1, 2004), at page 86.) We tend to agree.

COMMENT: The donor-managed account is designed to appeal to the donor who is reluctant to contribute because he feels the donee charity will not be able to match the investment results he (the donor) will obtain. One might view this as a device for the supremely self-confident. Those people do exist, of course, and this may appeal to them. However, for most donors, it will make more sense to run the investments in the donor's own name, and then contribute them later when they have gone up in value. ■